DICJ-IADI Round Table Opening Remarks

NAKAJIMA Junichi
Commissioner, Japan's Financial Services Agency (JFSA)
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(Introduction)

- Good afternoon, everyone. I am Junichi Nakajima, Commissioner of JFSA, Japan's Financial Services Agency.
- It is my great pleasure to have been given this opportunity to deliver my opening remarks. I would also like to express my sincere gratitude to Governor Mitsui and the Deposit Insurance Corporation of Japan for organizing this event.
- Today, let me speak a little bit about the history of the Japanese Deposit Insurance and challenges around financial supervision in the midst of Covid-19.

(History of the Japanese financial safety-net)

- More than 50 years have been passed since the Deposit Insurance Corporation of Japan was founded, and its role has become more and more important. One of the most significant events that influenced our Deposit Insurance system is the Japanese Financial Crisis from the late 1990s to the early 2000s.
- At that time, the Japanese banking safety-net and resolution scheme were not well-prepared for such an unprecedented crisis. Extensive parliamentary discussions led to the legislation of two important Acts in October 1998: namely, the Act on the Early Strengthening of Financial Functions and the Act on the Financial Reconstruction. These two acts allowed the government and the Deposit Insurance Corporation to precautionarily inject public funds into solvent banks, establish bridge banks, and temporarily nationalize banks.

As a deputy director, I contributed to these two legislations, pulling many all-nighters, and it is one of the highlights of my career.

- These legislations were originally planned to be temporary. However, they were incorporated into the Deposit Insurance act as permanent tools to swiftly address future bankruptcy. This formed the basis of the current banking safety net in Japan and resolution scheme for fighting financial crises.
- Afterwards, learning lessons from the Global Financial Crisis in 2008, the G20 endorsed the Key Attributes of Effective Resolution Regimes for Financial Institutions at the Cannes Summit in November 2011. We introduced resolution regimes aligned with the Key Attributes in 2013 and Total Loss-Absorbing Capacity (TLAC) framework in 2019 as well. Fortunately, as of today, we have never experienced a "bail-in" with these schemes in Japan, but we would like to continue discussions with overseas authorities, including today's participants, and Deposit Insurance Corporation in order to smoothly operationalize these resolution frameworks.

(Financial supervisory issues during the pandemic)

- Next, I would like to talk about Japanese financial supervisory issues that we face during the pandemic. Due to Covid-19, many businesses have been in a difficult situation. To support such firms, financial institutions play important roles in providing liquidity and facilitating business turn-around. From this viewpoint, I am going to mention three efforts that we are currently working on.

(Creation of sustainable business models)

- First, we are keen to focus on the sustainability of the financial institutions' business model amid dynamic societal changes. For financial institutions, holding strong capital positions is a prerequisite to supporting businesses. However, Japanese financial firms have been struggling due to the pandemic in addition to structural factors, such as the extended low interest rate

environment and aging society with declining birthrate. Regional financial institutions are particularly susceptible to these factors, and therefore the creation of sustainable business models is an urgent task for them.

- Taking this into consideration, JFSA has introduced the following three measures:
  - First, introducing a special act that exempts mergers and business integrations of regional banks from the application of the Anti-Monopoly Act under certain requirements.
  - Second, establishing a grant scheme for regional banks that will drastically improve their business efficiency through measures such as mergers and business integrations.
  - Third, amending the Banking Act to ease regulations on business scope and investments for diversifying businesses towards such fields as digitalization and regional revitalization.

  We will engage with financial institutions so that they can enhance their business foundations and contribute to the recovery of local economies after the pandemic, taking advantage of these measures.

(Abolition of "Inspection Manual" and reviewing the way of provisioning)

- Second, JFSA abolished the "Inspection Manual" and formulated a document titled "Concept and Policies for Inspection and Supervision of Loans after Discontinuance of the Inspection Manual" in December 2019. This new document highlights the importance of integrating a wide range of information, including future factors, into the evaluation of financial institutions' credit risks in their lending portfolio in addition to the past performance and qualitative/quantitative information of individual companies.
- Integrating various information into the assessment of credit risks is especially important in an uncertain business environment, notably during this pandemic. If banks recognize provisions in a timely and accurate manner,

they can support businesses more actively without fear of recurring additional losses.

- Against this background, some firms started to reconsider the way of provisioning along with their management strategy and lending policy. JFSA will engage with financial institutions so that they can maintain their soundness in an uncertain situation and contribute to the recovery of local economies by supporting customers through financial intermediation.

(A new collateral system looking ahead of a Post-Pandemic)

- Third, JFSA is reviewing the collateral system. The current Japanese collateral system limits collateral to individual assets, such as real-estate and tangible assets, and does not allow collateralizing the future cash-flow from a whole business.
- However, to create a business environment friendly to start-ups and facilitate business turnaround looking ahead to a Post-Pandemic future, it is desirable that companies, even those without tangible assets, can raise funds, by demonstrating their ability to generate cash-flow in the future. JFSA has been discussing with the Ministry of Justice to introduce a new collateral system covering businesses as a whole focusing on cash-flow, referencing overseas systems and practices.

(Closing)

- In conclusion, I sincerely hope that this conference, which has gathered many experts from deposit insurance institutions and other organizations all over the world, will be full of fruitful discussions and will contribute to making the global financial system more sound and stable. Thank you very much for listening.